Report

of the

Examination of

Mt. Pleasant-Perry Mutual Insurance Company

Monticello, Wisconsin

As of December 31, 2003

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State of Wisconsin / OFFICE OF THE COMMISSIONER OF INSURANCE

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October 1, 2004

Honorable Jorge Gomez
Commissioner of Insurance
State of Wisconsin
125 South Webster Street
Madison, Wisconsin 53702

Commissioner:

In accordance with your instructions, an examination has been performed as of December 31, 2003, of the affairs and financial condition of:

MT. PLEASANT-PERRY MUTUAL INSURANCE COMPANY
Monticello, Wisconsin

and the following report thereon is respectfully submitted:

I. INTRODUCTION

The previous examination of Mt. Pleasant-Perry Mutual Insurance Company (the company) was made in 1999 as of December 31, 1998. The current examination covered the intervening time period ending December 31, 2003, and included a review of such subsequent transactions deemed essential to complete this examination.

The "Summary of Examination Results" contains elaboration on all areas of the company's operations. Special attention was given to the action taken by the company to satisfy the recommendations and comments made in the previous examination report.

The company was organized as a town mutual insurance company on May 27, 1876, under the provisions of the then existing Wisconsin Statutes. The original name of the company was the Mt. Pleasant Fire Insurance Company. Subsequent amendments to the company's articles and bylaws changed the company's name to that presently used.

During the period under examination, there was no amendment to the articles of incorporation and no amendment to the bylaws.

The company is currently licensed to write property, including windstorm and hail, and nonproperty insurance. The company is currently licensed to write business in the following counties:

Columbia	Jefferson
Dane	Lafayette
Grant	Richland
Green	Rock
Iowa	Sauk

A review was made of the policy and application forms currently used by the company. The company issues approved policies with or without endorsements for terms of one year with premiums payable on the advance premium basis. The company also charges a billing fee of $2 for each semiannual and quarterly installment.

Business of the company is acquired through six agents, all of whom are directors of the company. Agents are presently compensated for their services as follows:

Type of Policy	Compensation
Property	12%
Nonproperty	12

Agents have authority to adjust losses up to $1,000. Losses in excess of this amount are adjusted by two agents. Losses that require significant expertise due to magnitude or complexity are handled by an outside adjuster. The adjusting committee will review losses on a monthly basis to ensure adequate evaluation and adjudication of claims. The committee will vote to approve payments for claims that are determined to financially impact the company. Agents receive $15 for each loss adjusted plus $0.32 per mile for travel allowance.

Policyholders may participate in the management and control of the company by attending and voting at all annual or special meetings of the members. No member may vote by proxy. The annual meeting of the company for the election of directors and special meetings of the company are held in accordance with its articles of incorporation.

Board of Directors

The Board of Directors consists of nine members divided into three classes. One class is elected at each annual meeting for a term of three years. Vacancies on the board may be filled by the directors for the interim to the next annual meeting when a director shall be chosen for the unexpired term. In 2004, the company experienced three management changes: the Office Manager resigned in May, a Director/Agent resigned in June and the Vice President, also a Director/Agent, retired in August. During the examination, the company had filled one of the two vacant director positions.

Changes made to the members of the Board of Directors are reflective of the company's intention to comply with the Wisconsin Statutes in regards to inside directors. Section 612.13 (1m), Wis. Stat., requires that the company limits the number of inside directors to be as follow:

(a) Beginning 2 years after April 30, 2004, all of the following apply:
   1. If a town mutual has fewer than nine directors, no more than one director may be an employee or representative of the town mutual.
   2. Employees and representatives of a town mutual may not constitute a majority of its board.

(b) Notwithstanding par. (a), the commissioner may allow a town mutual an extension of up to one year to come into compliance with the requirements under par. (a).

The company has additional plans to decrease the number of inside directors and expects to be in compliance with the statute when the statute takes effect.

The current Board of Directors consists of the following policyholders of the company:

Name	Principal Occupation	Residence	Expiry
Donald Elmer	Farmer	New Glarus, WI	2007
James Marty	Farmer	Monticello, WI	2007
Dennis Sutter *	Agent	Mt. Horeb, WI	2007
Charles Schriber*	Cattle Farmer/Agent	Hollandale, WI	2006
John Thornson*	Grocery Store Owner	Hollandale, WI	2006
Thomas Daly*	Green County Supervisor/Agent	Argyle, WI	2005
Otis Gilbertson*	Retired Farmer/Agent	Hollandale, WI	2005
Donald Roe*	Farmer	Belleville, WI	2005

Directors who are also agents are identified with an asterisk.

Members of the board currently receive $100 for each meeting attended with no allowance for travel expenses. Officers are paid $12 per hour plus $0.32 per mile travel allowance for each Executive Board Member meeting.

Officers

Officers are elected by the Board of Directors from among its members and hold office for one year or until their successors are duly elected and qualified. Officers serving at the present time are as follows:

Name	Office	Year Salary
Thomas Daly	President	$ 2,208
Vacant	Vice President	
Otis Gilbertson	Secretary	2,160
Dennis Sutter	Treasurer	1,638
Kathleen Grossen	Office Manager	29,120

Committees of the Board

The company's bylaws allow for the formation of certain committees by the Board of Directors. The committees at the time of the examination are listed below:

Adjusting Committee
Thomas Daly
Otis Gilbertson
Donald Roe
Charles Schriber
Dennis Sutter
John Thornson

Business Plan Committee
Thomas Daly
Otis Gilbertson
Kathleen Grossen
John Thornson

Financial Committee
Thomas Daly
Otis Gilbertson
Dennis Sutter
John Thornson

Growth of Company

The growth of the company since the previous examination as compiled from its filed annual statements was as follows:

Year	Net Premiums Earned	Policies In Force	Net Income	Admitted Assets	Policyholders' Surplus
2003	$793,831	2,181	$245,801	$2,440,810	$1,604,728
2002	732,082	2,066	13,889	2,209,169	1,377,314
2001	640,459	1,999	5,684	2,230,815	1,548,976
2000	612,838	1,961	(18,364)	2,268,897	1,579,410
1999	646,212	1,983	100,001	2,104,895	1,501,283
1998	595,890	2,018	(1,876)	2,014,897	1,406,458

The ratios of gross and net premiums written to surplus as regards policyholders since the previous examination are as follows:

Year	Gross Premiums Written	Net Premiums Written	Policyholders' Surplus	Writings Ratios	
				Gross	Net
2003	$1,443,407	$825,818	$1,604,728	90.0%	51.46%
2002	1,349,993	800,587	1,377,314	98.0	58.1
2001	1,261,758	669,385	1,548,976	81.5	43.2
2000	1,216,195	614,651	1,579,410	77.0	38.9
1999	1,220,331	649,254	1,501,283	81.3	43.3
1998	1,196,425	632,878	1,406,458	85.1	45.0

For the same period, the company's operating ratios are as follows:

Year	Net Losses and LAE Incurred	Other Underwriting Expenses Incurred	Net Premiums Earned	Loss Ratio	Expense Ratio	Com-posite Ratio
2003	$186,836	$325,064	$793,831	23.5%	41.0%	64.5%
2002	496,653	273,051	732,082	67.8	37.3	105.1
2001	439,180	256,481	640,459	68.6	40.1	108.6
2000	489,800	222,388	612,838	80.0	36.3	116.2
1999	398,391	219,157	646,212	61.7	33.9	95.6
1998	398,391	223,004	595,890	66.9	37.4	104.3

During the years under examination the company experienced generally favorable operating results and improving surplus position, despite its underwriting losses in three of the five years due to severe weather events in 2002 and 2001. The company had net income in each year except in 2000 when policy count was at its lowest and losses were increasing. Though not included in figures above, the company’s investment income contributed favorably to the company’s operating results in all years under examination. The company’s loss and expense ratios were usually comparable to or better than the average loss and expense ratios for all town mutuals during the examination period which were 60% and 43%, respectively.

II. REINSURANCE

The examiners' review of the company's reinsurance portfolio revealed there is currently one ceding treaty. The treaty contained a proper insolvency clause and complied with s. Ins 13.09 (3), Wis. Adm. Code, concerning maximum wind loss. Company retentions of risk complied with s. Ins 13.06, Wis. Adm. Code.

Reinsurer:	Wisconsin Reinsurance Corporation
Effective date:	January 1, 2004
Termination provisions:	Either party may terminate the contract and/or any of the attached Exhibit(s) at any January 1, by giving the other party at least 90 days' advance written notice.

The coverages provided under this treaty are summarized as follows:

1.	Type of contract:	Class A Casualty Excess of Loss
	Lines reinsured:	All casualty or liability business
	Company's retention:	$1,000 each and every loss occurrence
	Coverage:	100% of any loss, including loss adjustment expenses, above the company's retention in respect to each and every loss occurrence
	Reinsurance premium:	75% of premium written
2.	Type of contract:	Class B First Surplus
	Lines reinsured:	All property business
	Company's retention:	$400,000 per ceded risk or at least 50% on a pro rata basis per ceded risk when the company's net retention is $400,000 or less in respect to a risk. Additionally, the company retains an annual aggregate deductible equal to 10% of the loss and loss adjustment expenses otherwise recoverable.
	Coverage:	Up to $800,000 on a pro rata basis when the company's net retention is $400,000 or more in respect to a risk. When the company's net retention is $400,000 or less in respect to a risk, the company may cede on a pro rata basis up to 50% of such risk.
	Reinsurance premium:	Pro rata share of all premiums and fees charged by the company corresponding to the amount of each risk ceded.
	Ceding commission:	15% of premium paid and a profit commission of 15% of net profit, if any, accruing during each accounting period.

3.	Type of contract:	Class C-1 First Layer Excess of Loss
	Lines reinsured:	All property business
	Company's retention:	$35,000 per each and every loss resulting from one loss occurrence.
	Coverage:	100% of any loss, including loss adjustment expenses, in excess of $35,000 in respect to each and every risk resulting form one loss occurrence. Liability is limit to $65,000 in respect to each and every loss occurrence.
	Deductible:	Annual aggregate deductible of $30,000 (regardless of the number of claims involved)
	Reinsurance premium:	Based on experience over the past four years with load factor of 125%. Minimum rate: 6% of current net premiums written Maximum rate: 20.75% of current net premiums written Current rate: 6% Premium deposit: $6,250 Minimum premium for current year: $50,000
4.	Type of contract:	Class C-2 Second Layer Excess of Loss
	Lines reinsured:	All property business
	Company's retention:	$100, 000 per each and every loss resulting from one loss occurrence
	Coverage:	100% of any loss, including loss adjustment expense, in excess of $100,000, subject to a limit of liability to the reinsurer of $300,000.
	Reinsurance premium:	4.25% of the company’s current net premiums written in respect to the business covered. Premium deposit: $3,700 Minimum premium of $36,000
5.	Type of contract:	Class D/E First Aggregate Stop Loss & Catastrophe Coverage
	Lines reinsured:	All property business written
	Company's retention:	<u>Part A – Castrophe Coverage</u> $90,000 of net losses (excluding LAE) arising out of each loss occurrence. <u>Part B – Stop Loss Coverage</u> 75% of net written premium subject to a $673,000 minimum.
	Coverage:	<u>Part A – Castrophe Coverage</u> 100% of the amount by which the loss exceeds the retention, limited to $250,000 per any one loss occurrence and $500,000 per year.

Part B – Stop Loss Coverage
100% of the amount by which the aggregate of the company's net losses (including loss adjustment expenses) exceeds the retention.

Reinsurance premium: Based on experience over the past eight years with load factor of 125%.
Minimum rate: 8.5% of current net premiums written
Maximum rate: 25% of current net premiums written
Current rate: 9.73%
Premium deposit: $10,750
Minimum premium for current year: $88,000

III. AFFILIATED COMPANIES

The company is a member of a holding company system in which it is the ultimate parent. The organizational chart below depicts the relationship among an affiliate in the group. A brief description of the affiliate follows the organizational chart.

Mt. Pleasant-Perry Mutual Insurance Company
Monticello, Wisconsin

Mt. Pleasant-Perry Agency
Monticello, Wisconsin

In 1997, the company established Mt. Pleasant-Perry Agency, Inc., as an operating subsidiary. Initial capitalization of the agency consisted of a $10,000 cash contribution from the company. The agency was established to market auto liability and physical damage insurance underwritten by an affiliate of the company's reinsurer and to enable the company to offer automobile insurance to its insureds through the agency affiliate. Since 1997, the agency's product line has expanded to include umbrella and worker's compensation policies. The agency entered into a producer agreement with the auto insurer, under which the agency serves as an independent contractor engaged in the solicitation of insurance on behalf of the auto insurer.

The agency has one authorized agent, whose compensation consists of commissions of 7.5% on umbrella and worker's compensation policies, 12% on new auto policies written, and 9% on renewing policies and new policies written since May 1, 2004. The agency receives commission ranging from 6% to 15% of premiums written on its business lines solicited and contingency commission based on its three-year pure loss ratio. Commissions Revenue and Net Income reported was $20,565 and $9,659 (excluding dividend paid of $9,500), respectively, in 2003.

Prior to May 2004, the agency operated out of the company's home office. The agency had an office lease agreement and services agreement with the company in which the agent agreed to pay the company a specified fee under the agreements on a quarterly basis. In 2003, the agency paid the company a total of $450 in accordance with these agreements.

In May 2004, the company and the agency established an agreement whereby policyholder services are handled by the agency's appointed agent and all administrative services are provided by the agency's accountant. The agency's accountant is not an employee of the company. An independent accountant report prepared on an agreed-upon procedures basis was conducted as of February 29, 2004.

IV. FINANCIAL DATA

The following financial statements reflect the financial condition of the company as reported to the Commissioner of Insurance in the December 31, 2003, annual statement. Adjustments made as a result of the examination are noted at the end of this section in the area captioned "Reconciliation of Policyholders' Surplus."

Mt. Pleasant-Perry Mutual Insurance Company
Statement of Assets and Liabilities
As of December 31, 2003

Assets	**Ledger**	**Nonledger**	**Not Admitted**	**Net Admitted**
Cash in company's office	$ 100	$	$	$ 100
Cash deposited in checking account	1,000			1,000
Cash deposited at interest	1,208,307			1,208,307
Bonds	167,344			167,344
Stocks and mutual fund investments	802,808			802,808
Real estate	23,008			23,008
Premiums, agents' balances and installments:				
In course of collection	67,574			67,574
Deferred and not yet due	147,624			147,624
Investment income accrued		6,717		6,717
Reinsurance recoverable on paid losses and lae	7,160			7,160
Electronic data processing equipment	9,168			9,168
Furniture and fixtures	18,339		18,339	
Totals	$2,452,432	$6,717	$18,339	$2,440,810

Liabilities and Surplus

Net unpaid losses	$ 69,050
Unpaid loss adjustment expenses	1,625
Commissions payable	41,045
Fire department dues payable	757
Federal income taxes payable	96,115
Unearned premiums	507,503
Reinsurance payable	61,083
Payroll taxes payable (employer’s portion)	1,644
Other liabilities:	
Expense related:	
Accounts payable	4,334
Nonexpense related:	
Premiums received in advance	16,926
Total Liabilities	800,082
Policyholders' surplus	1,640,728
Total Liabilities and Surplus	$2,440,810

Mt. Pleasant-Perry Mutual Insurance Company
Statement of Operations
For the Year 2003

Net premiums and assessments earned		$793,831
Deduct:		
Net losses incurred	$151,449	
Net loss adjustment expenses incurred	35,387	
Other underwriting expenses incurred	325,064	
Total losses and expenses incurred		511,900
Net underwriting gain (loss)		281,931
Net investment income:		
Net investment income earned	60,136	
Net realized capital gains	(461)	
Total investment gain (loss)		59,675
Other income:		
Miscellaneous Income (Expense)	$ 310	
Total other income		310
Net income (loss) before federal income taxes		341,916
Federal income taxes incurred		96,115
Net Income (Loss)		$245,801

Mt. Pleasant-Perry Mutual Insurance Company
Reconciliation and Analysis of Surplus as Regards Policyholders
For the Five-Year Period Ending December 31, 2003

The following schedule is a reconciliation of surplus as regards to policyholders during the period under examination as reported by the company in its filed annual statements:

	2003	2002	2001	2000	1999
Surplus, beginning of year	$1,377,314	$1,548,976	$1,579,410	$1,501,283	$1,406,458
Net income	245,801	13,889	5,684	(18,364)	100,001
Net unrealized capital gains or (losses)	7,793	(164,569)	(33,570)	97,401	(3,441)
Change in non-admitted assets	9,820	(20,982)	(2,548)	(910)	(1,735)
Surplus, end of year	$1,640,728	$1,377,314	$1,548,976	$1,579,410	$1,501,283

Reconciliation of Policyholders' Surplus

The examination resulted in no adjustments to policyholders' surplus. The amount reported by the company as of December 31, 2003, is accepted.

V. SUMMARY OF EXAMINATION RESULTS

Compliance with Prior Examination Report Recommendations

Comments and recommendations contained in the last examination report and the action taken on them by the company are as follows:

1. Conflict of Interest—It is recommended that each of the company's officers, directors, and key employees annually make conflict of interest disclosures to the company, and that the company retains the disclosures in the company's records from examination to examination, incompliance with the directive of the Commissioner of Insurance.

   Action—Compliance.

2. Disaster Recovery Plan—It is recommended that the company develops a formal disaster recovery plan, to provide alternative plans and resources necessary for company business continuation in the event of significant business interruption.

   Action—Compliance.

3. Cash and Invested Cash—It is recommended that the company's cash deposits in any one banking institution does not exceed the maximum limitations of depository insurance provided to the depositors under available depository guaranty banking rules.

   Action—Compliance.

4. Net Unpaid Losses—It is recommended that the company ensure that all required data records for each claim reported to the company are assigned a claim number when reported, and are properly reported in the company's loss register and in its unpaid loss reports, so that each claim reported to the company is adequately documented so that amounts of settlement and coverage may be verified, in conformity with s. Ins 13.05 (4) (e), Wis. Adm. Code.

   Action—Compliance.

5. Reinsurance Payable—It is recommended that the company properly classify reinsurance balances in its statutory financial statements, and that the company report premium or commission overpayment recoverables and receivables as asset balances, in conformity with the annual statement page format and instructions.

   Action—Compliance.

6. Accounts Payable—It is recommended that the company properly classify its year-end payable liabilities, and that the reported accounts payable balance exclude amounts payable on unpaid losses, in compliance with annual statement instructions.

   Action—Compliance.

Current Examination Results

Corporate Records

The minutes of the annual meetings of policyholders and meetings of the Board of Directors and committees thereof, were reviewed for the period under examination and also for the subsequent period.

Biographical data relating to company officers and directors have been reported in accordance with the provisions of s. Ins 6.52, Wis. Adm. Code.

The company has executed formal written agreements with its agents. The contracts include language indicating the agent will represent the company's interests "in good faith."

Conflict of Interest

In accordance with a directive of the Commissioner of Insurance, each company is required to establish a procedure for the disclosure to its Board of Directors of any material interest or affiliation on the part of its officers, directors, or key employees which conflicts or is likely to conflict with the official duties of such person. A part of this procedure is the annual completion of a conflict of interest questionnaire by the appropriate persons. The company has adopted such a procedure for disclosing potential conflicts of interest. Conflict of interest questionnaires were reviewed for the period under examination. Directors who were agents disclosed this as a potential conflict; no other apparent conflicts were noted.

Fidelity Bond and Other Insurance

The company is afforded coverage under the terms of the following bonds or contracts and has complied with s. Ins 13.05 (6), Wis. Adm. Code, which sets forth the minimum requirements for fidelity bond coverage:

Type of Coverage	Coverage Limits
Fidelity bond	$250,000
Workers Compensation:	
Employee injury	Statutory
Employee liability:	
Each accident	100,000
Each employee	100,000
Policy limit	500,000
Commercial Coverage:	
Property:	
Deductible	500
Building	145,700
Personal property	25,000
Equipment breakdown	25,000
General Liability:	
General aggregate	1,000,000
Each occurrence	1,000,000
Personal and advertising	1,000,000
Medical (any one person)	5,000
Inland Marine:	
Accounts Receivable	10,000
Hardware	27,500
Deductible	250
Insurance Company Combined:	
Professional Liability:	
Deductible	5,000
Each Claim	5,000,000
Aggregate	5,000,000
Directors & Officers Liability:	
Deductible	5,000
Each Claim	5,000,000
Aggregate	5,000,000
Policy Maximum	5,000,000
Errors and Omissions:	
Deductible	1,500
Each claim per agent	1,000,000
In Aggregate	1,000,000

Underwriting

The company has a written underwriting guide. The guide covers all the lines of business that the company is presently writing.

The company has a formal inspection procedure for both new and renewal business. A sampling of new applications and renewal business is inspected by committee members who are independent of the risk under consideration and review.

In accordance with the Class B provision discussed in the “Reinsurance” section of this report, for policies with coverage in excess of the company’s retention, the company must submit a ceding slip to the reinsurer to determine the pro rata share of each policy. The company’s guideline states that at renewal and for endorsements, new ceding slips are to be submitted when change in coverage exceeds $10,000. During the review of the company’s 10 largest risks, the examiners noted that ceding slips for four policies with coverage in excess of Class B reinsurance retention were not updated to reflect the change in coverage when change was in excess of $10,000.

In addition, in the General Interrogatories of the Annual Statement, the largest fire risk insured by the company was reported to be $2,085,000. The company used a report from its reinsurer on ceded pro rata coverage as of December 31, 2003, to determine the largest fire risk. The policy for this risk was reviewed and determined that at year-end the total fire risk for this policy was only $1,738,300; the difference is $346,700. The largest fire risk reported should have been $2,009,200 for a different policyholder. The reinsurer’s report is based on information provided by the company through ceding slips. It is recommended that the company take action to ensure that all ceding slips are updated to reflect any policy changes over $10,000. It is recommended that the largest fire risk insured by the company is accurately reported on the annual statement.

Claims Adjusting

The company has an adjusting committee consisting of at least three directors as required by s. 612.13 (4), Wis. Stat. The function of this committee is to adjust or supervise the adjustment of losses.

The adjusting committee meets on a monthly basis. The company office manager provides the committee a list of all unsettled claims at each meeting. Examiner review of board minutes noted that the board exercised appropriate procedures to evaluate and approve payments on losses that would have a financial impact on the company. The company appears to have effective standards and practices for the mitigation of losses.

Accounts and Records

The examiners' review of the company's records indicated that the company is in compliance with s. Ins 13.05, Wis. Adm. Code, which sets forth the minimum standards for the handling of cash and recording of cash transactions by town mutual insurance companies. The examiners noted the following:

1. A proper policy register is maintained
2. A proper cash receipts journal is maintained
3. A proper cash disbursements journal is maintained
4. A proper general journal is maintained
5. A proper general ledger is maintained

An extensive review was made of income and disbursement items. Cash receipts were traced from source records and the proper recording and eventual deposit thereof ascertained. Negotiated checks issued during the period under examination were reviewed, test checked for proper endorsement, and traced to cash records. The verification of assets and determination of liabilities were made as of December 31, 2003.

The company is audited annually by an outside public accounting firm.

EDP Environment

Company personnel were interviewed with respect to the company’s electronic data processing environment. Access to the computers is limited to people authorized to use the computers.

Company personnel back up the computers daily and the backed-up data is kept off-site. Year-end back-ups are kept at the company’s bank safety deposit box.

A manual which describes how to use the company’s software and outlines the steps to complete specific tasks assists in the continuity of operations for seldom-used applications, training, or when staff turnover occurs. The company has manuals documenting the use of its software.

Business Continuity Plan

A business continuity plan identifies steps to be performed by a company in the event of business interruptions including, but not limited to, the inability to access its computer, the loss of information on its computer, the loss of a key employee, or the destruction of its office building. The company has developed a business continuity plan. The company's business continuity plan appears to be adequate.

Invested Assets

Section 610.23, Wis. Stat., requires insurers to hold all investments and deposits of its funds in its own name except that:

(1) Securities kept under a custodial agreement or trust arrangement with a bank or banking and trust company may be issued in the name of a nominee of the bank or banking and trust company; and

(2) Any insurer may acquire and hold securities in bearer form.

For securities not held under a custodial agreement or trust arrangement with a bank or banking and trust company, s. Ins 13.05 (4), Wis. Adm. Code, requires that:

> Non-negotiable evidences of company investments such as registered bonds, certificates of deposits, notes, etc., shall be maintained in a safe or vault with adequate safety controls or in a safety deposit box in a bank. Negotiable evidences of company investments shall be maintained in a safety deposit box in a bank. Access to a company safety deposit box containing negotiable securities shall require the presence and signature of at least 2 officers, directors or employees of the company.

The company is not in compliance with these requirements. The company has a safekeeping agreement with a local bank that holds all of its investments with an exception to certificates of deposit. However, it was noted that the company has two certificates of deposit held by a broker totaling $95,000. It is recommended that the company have all investments held by the broker transferred and held by the custodian pursuant to s. 610.23, Wis. Stat., and s. Ins 13.05 (4) (f) Wis. Adm. Code.

Investment Rule Compliance

The investment rule for town mutual insurers allows a company to invest in common stocks, common stock mutual funds, and other higher risk investments (referred to as "Type 2") provided that the town mutual has a sufficient amount of lower risk investments (referred to as

“Type 1”). A town mutual may invest in Type 2 securities only if it already has sufficient Type 1 investments. Type 1 investments must equal or exceed the greater of items 1, 2, or 3.

1.	Liabilities plus $300,000	$1,100,082
2.	Liabilities plus 33% of gross premiums written	1,276,406
3.	Liabilities plus 50% of net premiums written	1,212,991
4.	Amount required (greater of 1, 2, or 3)	1,276,406
5.	Amount of Type 1 investments as of 12/31/2003	1,379,938
6.	Excess or (deficiency)	$ 103,532

The company has sufficient Type 1 investments.

The company was granted an exception to hold up to 40% of its assets in common stocks, preferred stocks and mutual funds.

ASSETS

Cash and Invested Cash **$1,209,407**

The above asset is comprised of the following types of cash items:

Cash in company's office	$ 100
Cash deposited in banks-checking accounts	1,000
Cash deposited in banks at interest	1,208,307
Total	$1,209,407

Cash in the company's office at year-end represents the company's petty cash fund. A physical count was made by the examiners during the course of the examination. The examiners noted that petty cash is larger than that reported above. The variance was determined to be below tolerable error; however, the company indicated that petty cash has always been more than that reported on the Annual Statement. It is recommended that the company report the correct balance of all accounts on its Annual Statement, including petty cash.

Cash deposited in banks subject to the company's check and withdrawal consists of two accounts maintained in one bank. Verification of checking account balances was made by obtaining confirmations directly from the depository and reconciling the amounts shown thereon to company records.

Cash deposited in banks represents the aggregate of fifteen deposits in fourteen depositories. Thirteen of the deposits were verified by direct correspondence with the respective depositories and by an actual count and inspection of certificates and/or passbooks. Two of the deposits were not verified by a direct correspondence with its respective depository, but were traced to a broker statement. Investments held by a broker are not in compliance with s. 610.23, Wis. Stat., and s. Ins 13.05 (4), Wis. Adm. Code, in regards to holding all investments and deposits of its funds in its own name as discussed under the “Invested Assets” section of this report.

Interest received during the year 2003 totaled $40,995 and was verified to company cash records. Rates of interest earned on cash deposits ranged from 1.10% to 5.50%. Accrued interest on cash deposits totaled $4,230 at year-end.

Book Value of Bonds **$167,344**

The above asset consists of the aggregate book value of bonds held by the company as of December 31, 2003. Bonds owned by the company are held by the company's custodian. Bond purchases and sales for the period under examination were checked to brokers' invoices and advices. The company's investment in bonds was in conformance with Wisconsin Statutes and the rules of the Commissioner of Insurance as regards investments made by town mutual insurers.

Interest received during 2003 on bonds amounted to $5,493 and was traced to cash receipts records. Accrued interest of $2,487 at December 31, 2003, was checked and allowed as a nonledger asset.

Stocks and Mutual Fund Investments **$802,808**

The above asset consists of the aggregate market value of stocks and mutual funds held by the company as of December 31, 2003. Stocks owned by the company are held by the custodian. Stock and mutual fund purchases and sales for the period under examination were checked to brokers' invoices and advices. The company's investment in stocks and mutual funds was in conformance with Wisconsin Statutes and the rules of the Commissioner of Insurance as regards investments made by town mutual insurers.

Dividends received during 2003 on stocks and mutual funds amounted to $30,308 and were traced to cash receipts records.

Book Value of Real Estate **$23,008**

The above amount represents the company's investment in real estate as of December 31, 2003. The company's real estate holdings consisted of the company's home office.

The required documents supporting the validity of this asset were reviewed and were in order. Adequate hazard insurance was carried on the real estate and contents as noted under the caption, "Fidelity Bond and Other Insurance." The company's investment in real estate and related items was in conformance with the Wisconsin Statutes and the rules of the Commissioner of Insurance as regards investments made by town mutual insurers. Real estate depreciation is calculated using the MACRS accelerated depreciation method.

Premiums, Agents' Balances in Course of Collection **$67,574**

This asset represents the amounts due from agents or policyholders which are not in excess of 90 days past due at year-end. A review of individual agent's accounts verified the accuracy of this asset.

Premiums Deferred and Not Yet Due **$147,624**

This asset represents modal premium installments (such as monthly, quarterly, etc.) that are not yet due. A review of a sample from the company's detailed list of deferred premiums verified the accuracy of this asset.

Investment Income Due and Accrued **$6,717**

Interest due and accrued on the various assets of the company at December 31, 2003, consists of the following:

Cash at Interest	$4,230
Bonds	2,487
Total	$6,717

Reinsurance Recoverable on Paid Losses **$7,160**

The above asset represents recoveries due to the company from reinsurance on losses which were paid on or prior to December 31, 2003. A review of year-end accountings with the reinsurer verified the above asset.

Electronic Data Processing Equipment **$9,168**

The above balance consists of computer hardware and operating system software, net of depreciation as of December 31, 2003. A review of receipts and other documentation verified the balance. Non-operating system software was properly nonadmitted.

Furniture and Fixtures **$0**

This asset consists of $18,338 of office furniture, equipment and software owned by the company at December 31, 2003. In accordance with annual statement requirements, this amount has been reported as nonadmitted asset, thus the balance shown above is $0.

LIABILITIES AND SURPLUS

Net Unpaid Losses **$69,050**

This liability represents losses incurred on or prior to December 31, 2003, that remained unpaid as of that date. The examiners reviewed the reasonableness of this liability by totaling actual loss payments made subsequent to December 31, 2003, with incurred dates in 2003 and prior years. The examiners' development of unpaid losses is compared with the amount estimated by the company in the following schedule.

	Company Estimate	Examiners' Development	Difference
Incurred but unpaid losses	$156,529	$137,694	$18,835
Less: Reinsurance recoverable on unpaid losses	87,479	82,381	5,098
Net Unpaid Losses	$ 69,050	$ 55,313	$13,737

The above difference of $13,737 resulted from the company’s conservative estimates for two fire claims that have settled and five liability claims closed without payment in 2004. No adjustment was made to the unpaid losses reserve because the difference was not considered material.

The examiners' review of claim files included open claims, paid claims, claims closed without payment, and all claims which were denied during the examination period. The review indicated that claims are investigated and evaluated properly and that payments are made promptly and in accordance with policy provisions upon the submission of a proper proof of loss. In addition, the review of claims handling procedures and files revealed the following:

1. A proper loss register is maintained.
2. Claim files contain sufficient investigatory data and documentation to verify settlement payments or reserve estimates.
3. Proofs of loss were properly signed.

The examination also noted that the company did not always send a written claim denial after a verbal denial was given for claims closed without payment. It is an unfair claim settlement practice to fail to affirm or deny coverage of claims within a reasonable time, pursuant to s. Ins 6.11 (3) (a) 7, Wis. Adm. Code. In order to document files, and to avoid the unfair claims settlement practices described in s. Ins 6.11 (3) (a) 7, Wis. Adm. Code, it is suggested that the company implement procedures to send a written claim denial promptly after a claim is verbally denied.

Unpaid Loss Adjustment Expenses **$1,625**

This liability represents the company's estimate of amounts necessary to settle losses which were incurred prior to December 31, 2003, but which remained unpaid as of year-end. The methodology used by the company in establishing this liability relies on the independent auditor's estimates based primarily on open claims and estimated IBNR claims multiply by $25 average fee per claim.

The examiners' analysis of expenses incurred in the current year related to the settlement of prior year losses, as well as estimates of amounts necessary to settle any prior losses remaining unpaid at the examination date, determined this liability to be adequately stated.

Commissions Payable **$41,045**

The above liability represents unpaid commissions due to the company's director/agents on premiums for policies written and in effect on or prior to December 31, 2003. A review of the company's agents' commission records and 2004 cash disbursements verified the reported year-end balance.

Fire Department Dues Payable **$757**

This liability represents the fire department dues payable at December 31, 2003. The examiners reviewed the company's fire department dues calculation and found this liability to be correctly calculated. The actual amount paid was verified to the cash disbursement records.

Federal Income Taxes Payable **$96,115**

This liability represents the balance payable at year-end for federal income taxes incurred prior to December 31, 2003. The examiners reviewed the company's 2003 tax return and verified amounts paid to cash disbursement records to verify the accuracy of this liability.

Unearned Premiums **$507,503**

This liability represents the reserve established for unearned premiums in compliance with s. Ins 13.08 (3), Wis. Adm. Code. This reserve was established using a daily pro rata methodology, which computes the unearned portion of premium for each respective policy in force at year-end, based on the amount of premium in force, the policy inception date and expiration date, and the mode of premium payment. Testing of policy data and recalculation verified the unearned premium liability balance reported as of year-end.

Reinsurance Payable **$61,083**

This liability consists of amounts due to the company's reinsurer at December 31, 2003, relating to transactions which occurred on or prior to that date. Subsequent cash disbursements and reinsurance accountings verified the amount of this liability.

Payroll Taxes Payable **$1,644**

This liability represents the company's portion of payroll taxes incurred prior to December 31, 2003, which had not yet been paid. Supporting records and subsequent cash disbursements verified this item.

Accounts Payable **$4,334**

The account payable liability represents amounts due and accrued at year-end for miscellaneous expense items, including accounting expense, office supplies and utilities. Supporting records and subsequent cash disbursements verified this item.

Premiums Received in Advance **$16,926**

This liability represents the total premiums received prior to year end for policies with effective dates after December 31, 2003. The examiners reviewed 2004 premium and cash receipt records to verify the accuracy of this liability.

VI. CONCLUSION

During the period, Net Premium Written increased by 27.2%, total Admitted Assets increased by 21.1% and Surplus increased by 9.3%. There were no adjustments to Surplus as the result of the examination.

The examination resulted in four recommendations and one suggestion. The recommendations relate to underwriting, invested assets and cash and invested cash. The suggestion relates to the company's claims procedures.

The current examination finds that the company is financially sound, although the company had three years of underwriting loss in the period under examination. The company's 2003 loss and expense ratios are lower than the average ratios of all town mutuals. The company's accounts and records are in good order, despite the recent changes to management, and the attentiveness of the company's personnel during the examination was greatly appreciated.

VII. SUMMARY OF COMMENTS AND RECOMMENDATIONS

1. Page 19 - Underwriting—It is recommended that the company take action to ensure that all ceding slips are updated to reflect any policy changes over $10,000.

2. Page 19 - Underwriting—It is recommended that the largest fire risk insured by the company is accurately reported on the annual statement.

3. Page 21 - Invested Assets—It is recommended that the company have all investments held by the broker transferred and held by the custodian pursuant to s. 610.23, Wis. Stat., and s. Ins 13.05 (4) (f) Wis. Adm. Code.

4. Page 23 - Cash and Invested Cash—It is recommended that the company report the correct balance of all accounts on its Annual Statement, including petty cash.

5. Page 26 - Claims Procedures—In order to document files, and to avoid the unfair claims settlement practices described in s. Ins 6.11 (3) (a) 7, Wis. Adm. Code, it is suggested that the company implement procedures to send a written claim denial promptly after a claim is verbally denied.

VIII. ACKNOWLEDGMENT

The courteous cooperation extended to the examiners by the company's personnel is hereby acknowledged.

In addition to the undersigned, Dave Grinnell of the Office of the Commissioner of Insurance, State of Wisconsin, participated in the examination.

Respectfully submitted,

Sheur Yang
Examiner-in-Charge